

# Coleman & Horowitz Real Estate Memo

Discussing Issues of Interest to our Clients

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## COURT DEFINES DUTY OWED BY AGENTS AND SELLERS TO BUYERS

By Darryl J. Horowitz

On August 13, 1997, the Fourth District Court of Appeal handed down its decision in *Robinson v. Grossman* (1997) 57 Cal.App.4th 1163, 97 Daily Journal D.A.R. 11613. In that decision, the court held that a real estate agent cannot be held liable for reasonably relying on representations made by a seller in connection with the agent's duty to disclose.

The court has recently provided further insight as to the duty of an agent and owner in making disclosures to potential purchasers. This memorandum will discuss two recent cases which provide clarification as to the potential liability of an agent for reliance on representations made by a seller and the seller's liability for representations: *Pagano v. Krohn*, 97 Daily Journal D.A.R. 15195 (November 17, 1997) and *Shapiro v. Sutherland*, 98 Daily Journal D.A.R. 137 (January 5, 1998).

### ***Pagano v. Krohn***

In *Pagano v. Krohn*, the court held that an agent is not liable when he/she relies on the representations of the seller, the buyer has an opportunity to properly inspect the property and the inspection does not reveal any deficiencies. In order to understand the court's decision, however, an understanding of the facts is important.

### **Facts**

In April of 1996, Helga Krohn listed her condominium in Black Horse Ranch for sale with

Peggy Chodrow, an agent with Coldwell Banker Residential Real Estate Corporation. In connection with the sale, Krohn prepared a transfer disclosure statement, in which she stated that while the development is on leased land and other units have experienced water intrusion problems, she was unaware of any flooding, grading, draining or water intrusion problems.

Raymond Pagano, represented by Jim Lawson, made an offer on the property. In connection with the offer, Lawson inspected the property and found no evidence of water intrusion, noting that "This home seems to be in good shape. I recommend Buyer have the property inspected prior to the close of escrow." Lawson was also advised that other units in the development had water intrusion problems, but not Krohn's unit.

The sale did not go through and escrow was canceled, after which the association sent an update to Krohn on the water intrusion problem. The update advised the owners that a lawsuit had been filed against the developer and settlement negotiations were underway.

Pagano then made another offer (\$5,000 less than the original offer), which was accepted. In addition to the information previously provided, Krohn provided Pagano with the association's update letter. Pagano then hired an inspector and accompanied the inspector during his four-hour inspection. Neither the inspector nor Pagano found any evidence of water damage. The escrow was thus closed. A few months after

the close of escrow, an engineer installing a sound system found evidence of water damage; i.e., dry rot and dampness in an area in which carpet and the base board had been removed. Pagano then sued Krohn, Chodrow, Coldwell Banker and Lawson for various causes of action, including rescission, breach of contract and fraud.

The defendants filed a motion for summary judgment on the grounds that none of the parties was aware of any water intrusion and that they had met all of their duties of disclosure. The trial court agreed, granting the motion. In doing so, the court ruled that “[A]s a matter of law, the court finds that the real estate brokers are only required to disclose problems with a unit that could have been discovered through a visual inspection.”

### The Ruling

The appellate court agreed with the trial court, finding that the real estate agents had met their obligations by passing along the information regarding the water intrusion problems experienced by other owners. The court focused on what it felt was the key issue, namely, whether Pagano was informed that other units in the development experienced a water intrusion problem. The court found that Pagano did have such knowledge.

Although Pagano argued that Krohn and her agent should have disclosed the extent of her knowledge of the water intrusion problem (i.e., 31 documents from the association, personal knowledge of three owners with water intrusion problems, and her reading of the lawsuit), the court was unpersuaded, stating:

“Disclosure of these additional facts would have served only as elaboration on the basic disclosed fact that there was a water intrusion problem in the development affecting some of the units and resulting in a lawsuit against the developer. There is no evidence in the record that at the time the Paganos purchased their unit Chodrow had reason to believe the problem would affect every

unit in the development. . .” (97 Daily Journal D.A.R. at 15197.)

The court also found that a review of the association’s materials and the lawsuit would not have added anything more significant as they did not disclose a water intrusion problem in Krohn’s unit, and in doing so stated:

“[T]he Paganos knew there was water intrusion at Blackhorse which had resulted in litigation against the developer. The additional details they fault Chodrow for not disclosing, including the content of the Association’s complaint, were within their own diligent attention.” (*Ibid.*)

The court then to discussed the lack of liability on the part of the owner or Pagano’s agent. The court found that although the owner had experienced algae and efflorescence in the past, Pagano had failed to show the relevance of such and found that the owner had given sufficient information from which Pagano could make a decision.

In discussing Lawson’s lack of liability, the court stated:

“When the buyer’s agent transmits material information from the seller to the buyer, the agent must either verify the information or disclose to the buyer that it has not been verified. [Cit. Om.] Accordingly, a buyer’s agent is not required to verify information received from the seller and passed on to the buyer if the buyer understands the agent is merely passing on unverified information. [Cit. Om.]” (97 Daily Journal D.A.R. at 15198.)

The court also found that Lawson had not breached his duty of disclosure by not disclosing his knowledge that a lawsuit would decrease the value of the property, stating:

“[C]onclusions as to how the legal or practical ramification of disclosed facts adversely impact value are not ‘facts’

subject to an agent's duty of

disclosure. [Cit. Om.]" (*Ibid.*)

### ***Shapiro v. Sutherland***

In *Shapiro v. Sutherland*, the Second District Court of Appeals held that an owner has a duty under "common law" to disclose problems the owner had with a noisy neighbor. The Court refused, however, to find that the relocation company that ultimately sold the property did not have a duty to make such a disclosure in the absence of any knowledge of the noise problem.

### **Facts**

Sutherland was the owner of property in Burbank. As part of a transfer from California to Washington, his employer arranged for the purchase of his house by Prudential Relocation Management, a relocation service. The relocation service obtained a transfer disclosure statement from Sutherland which did not disclose any deficiencies.

Prudential then entered into an agreement to sell the property to the plaintiff, Shapiro. In connection with the sale of the property, Shapiro signed an addendum submitted by Prudential whereby Shapiro acknowledged that Prudential had never occupied the property and the property was being sold as is. It also recommended that Shapiro conduct any inspections he felt were necessary. The sale then closed.

Unbeknownst to either Prudential or Shapiro, while the Sutherlands lived at the property, they experienced noise and disturbance problems with their neighbors, the Williamses, such that they called the police on several occasions. This was not included on any disclosure form.

After Shapiro moved into the property, he too experienced noise and disturbance problems that he could not rectify. He then provided Prudential with notice that he wished to rescind the sale. Prudential declined and Shapiro filed a lawsuit.

At the trial court, both Sutherland and

Prudential filed motions for summary judgment: Sutherland on the grounds that he had no duty to make such a disclosure and Prudential on the ground that it had no notice of the noise problems and thus had no duty to disclose such. The trial court granted the motions and Shapiro appealed.

### The Ruling

The court reversed the lower court, holding that under both common law and statutes that relate to disclosures required in connection with real estate transactions (Civil Code §§ 1102.6, et seq.), Sutherland had a duty to disclose problems they may have had with noisy neighbors. As to the common law duties of disclosure, the court held:

“In the context of a real estate transaction, ‘[i]t is now settled in California that where the seller knows of facts materially affecting the value or desirability of the property. . .and also knows that such facts are not known to, or within the reach of the diligent attention and observation of the buyer, the seller is under a duty to disclose them to the buyer. [Citations.]’ [Citations omitted.]” (97 Daily Journal D.A.R. 137, 140.)

The court noted that under Civil Code § 1102.6, a seller has an affirmative duty to state whether he/she is aware of “neighborhood noise problems or other nuisances” and if the seller is aware of such, to describe the problem. (*Ibid.*) Since Sutherland had a duty to complete the transfer disclosure statement in “good faith”, which is defined as “honesty in fact in the conduct of the transactions” (*Ibid*, citing Civil Code § 1102.7).

The court found that Sutherland *did* have an obligation to disclose the noisy neighbor problem.

The court then turned to Prudential’s liability and found that they did not have liability for misrepresentation. The court found that since Prudential produced uncontroverted evidence that it had no knowledge of the noise problems, and properly advised the buyer that Prudential

knew nothing about the property and Sutherland agreed to do his own investigation, Prudential had met its duty and thus had no liability for misrepresentation. The court, nevertheless, held that since Shapiro had requested rescission (i.e., that the deal be undone), Prudential was a necessary party and thus should not be dismissed.

### Conclusion

These decisions remind us that when in doubt, disclose. *Pagano* teaches us that the transmittal of information received from the seller is essential in every transaction, as doing so may prevent liability.

*Shapiro* serves as an excellent reminder of the duty of the seller -- often overlooked as the necessary key to obtaining accurate information regarding condition of property -- to truthfully disclose all pertinent information, even if it deals with a personality conflict with a neighbor. In fact, the court noted that even though Sutherland was not the direct seller, he still had liability because it was reasonable to assume that the information he provided on the transfer disclosure statement would be relied upon by subsequent sellers. (98 Daily Journal D.A.R. 137, 141-2; citing Restatement Second of Torts § 533 and *Greenbaert v. Mitchell* (1955) 31 Cal.App.4th 601.)

Where you are not sure whether you should disclose information relating to real property, think carefully about withholding the information, and remind sellers of their duty to disclose. Failure to do so could land you in court without a defense to a suit for failure to disclose, whereas complete disclosure may give you the defense you need.

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